

Analysis of  
Business  
Trends Plus  
Selected  
Financial  
Indicators

## Despite Lower Mortgage Rates . . .

When mortgage interest rates approached single-digit levels early last year, many people assumed that housing starts and sales would return to levels near those reached during the halcyon days of the 1970s—the last time rates were so low. However, although residential construction has risen to respectable levels during the four years after the housing slump of 1981 and 1982, the monthly annualized level of housing starts has rarely topped two million units, and no annual total has come even close to the 1972 record of 2.36 million homes started.

What makes this less than spectacular performance more curious is that it comes not only during a period of falling interest rates, but also at a time when twice as many Americans than in the early 1970s are in the 25 to 34-year age group when first homes are usually bought. Yet, in spite of these two favorable factors, housing starts fell in eight out of the first 11 months of 1986, and new single-family home sales in the third-quarter 1986 were 5.8 percent below year-earlier levels.

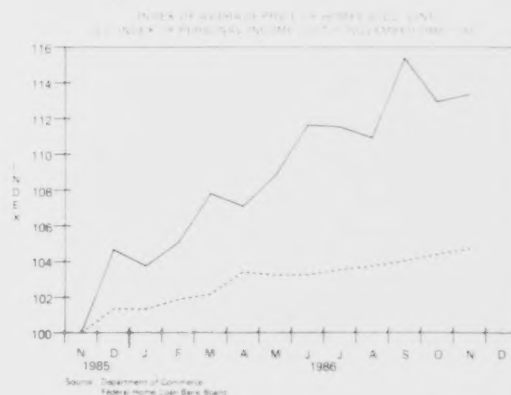
Certainly, the new tax laws are holding back construction of multifamily units—projects that in recent years have tended to be speculative developments or tax shelters. And the energy sector's problems in the South and Southwest have reduced demand in areas where homes were being erected at a furious pace just a few years earlier. Nonetheless, even after adjusting for these developments, housing is not reaching the levels that might normally be expected at today's interest rates.

The problem in housing does not seem to be demand. Given existing demographics and housing stock, at least 1.9 million additional units will be needed each year over the next four years. The problem appears to be that rising home prices have far outpaced any compensating drop in mortgage rates or growth in personal income. While the average U.S. interest rate on a mortgage dropped to 9.87 percent in November 1986 from 11.20 percent a year earlier, the price of a mortgaged home surged by 13.3 percent. By comparison, personal income

rose only 4.7 percent during the same period (see chart).

## . . . Many Americans Are Still Unable . . .

The upward rise in mortgages is visible in many major cities across the U.S. Using third-quarter 1986 data supplied by the Federal Home Loan Bank Board, monthly mortgage payments can be estimated in the 32 urban areas that contain half the population of the U.S. In 12 of these 32 areas, monthly payments rose despite the fact that interest rates fell in nearly all cities. The rise was greatest in the Portland, Oregon area, where monthly payments rose an astounding \$100 in just a year's time mainly because of a 33-percent jump in the price of a mortgaged home. Still, at an estimated \$769 a month, Portland's average monthly mortgage payment would appear to be more manageable than the \$1,158 payment needed in San Francisco, or the \$1,103 required in Washington, D.C.



Although economic conditions, such as the energy problems in Dallas, did depress home prices in three areas from third-quarter 1985 to third-quarter 1986, in 18 cities prices jumped by double-digit rates as better employment prospects pushed up demand. In the rapidly growing Boston area prices rose 10.2 percent; in the New York City region, the average home sold for 16 percent more than a year earlier. And in Indianapolis, which added almost 25,000 jobs and where the unemployment rate fell a full percentage point over the past year, home prices rose 23 percent.

Manufacturers  
Hanover  
Economics  
Department  
17-270

### ... To Afford Their Own Homes

Obviously, the old rule of thumb that a quarter of one's income should go toward housing costs is falling by the wayside. What is more, homebuyers are employing various techniques to offset—at least in part—the upward trend of home prices and mortgage payments. One method is a larger down payment, which explains why the New York City area's payment rose by only \$5 in a year. Buyers in the region covered more than one third of the purchase price of their homes with a sizable down payment, thus holding their monthly mortgage bill to only \$967, the seventh highest figure in the U.S.

This is the case even though the area covering New York, New Jersey and Connecticut had the second highest price of a mortgaged home, \$161,000.

Another option is to stretch out the mortgage maturity period, a practice most prevalent in the West. For other buyers, "settling" for a smaller house or one with fewer amenities is the way to achieve the American dream of homeownership. Still, as long as the rise in home prices and corresponding mortgage payments outpace growth in income, the pursuit of homeownership

### Short Term Paper Outstanding

(Millions of Dollars)

| Time Deposits of \$100,000 or more<br>Weekly Reporting Banks | Latest Week | Change Since |          |
|--------------------------------------------------------------|-------------|--------------|----------|
|                                                              |             | Week Ago     | Year Ago |
| Nationwide (12/17/86)                                        | 151,348     | — 507        | — 7,177  |
| New York City (12/17/86)                                     | 34,093      | — 136        | — 347    |
| Commercial Paper (12/17/86)                                  | 325,562     | + 588        | + 32,401 |

### Bank Loans

(Millions of Dollars)

| Commercial and Industrial Loans         |             |              |          |
|-----------------------------------------|-------------|--------------|----------|
| Weekly Reporting Large Commercial Banks | Latest Week | Change Since |          |
|                                         |             | Week Ago     | Year Ago |
| Nationwide (12/17/86)                   | 268,994     | + 3,030      | + 12,485 |
| New York City (12/17/86)                | 62,323      | + 559        | + 3,396  |
| Total Loans and Leases Gross Adjusted   |             |              |          |
|                                         | Latest Week | Change Since |          |
|                                         |             | Week Ago     | Year Ago |
| Nationwide (12/17/86)                   | 769,005     | + 6,005      | + 52,055 |
| New York City (12/17/86)                | 169,029     | + 240        | + 10,097 |

### Financial Markets

| Financial Markets                            | Wednesday<br>12/31/86 | Change Since |         | Year<br>Ago |
|----------------------------------------------|-----------------------|--------------|---------|-------------|
|                                              |                       | Week<br>Ago  |         |             |
| U.S. Governments, Closing Yields:            |                       |              |         |             |
| 90-Day Bills †                               | 5.80%                 | +            | .10     | — 1.49      |
| 180-Day Bills †                              | 5.84                  | +            | .04     | — 1.64      |
| Longest Bills †                              | 5.92                  | +            | .05     | — 1.71      |
| Recent Issues:                               |                       |              |         |             |
| 61/4s 12/31/88 (When Issued)                 | 6.32                  | +            | .07     |             |
| 65/8s 12/31/90 (When Issued)                 | 6.72                  | +            | .11     |             |
| 71/4s 11/15/96                               | 7.23                  | +            | .16     |             |
| 71/2s 11/15/16                               | 7.48                  | +            | .15     |             |
| Municipals:                                  |                       |              |         |             |
| Bond Buyer—20 Bond Index*<br>(12/18/86)      | 6.92%                 | —            | .02     | — 1.46      |
| Blue List Total (\$ Million)                 | \$2,598               | — \$         | 76      | +\$ 818     |
| 30-Day Visible Supply<br>(\$ Million)        | \$1,054               | —            | \$2,431 | +\$ 517     |
| Total                                        | \$3,652               | —            | \$2,507 | +\$1,335    |
| Corporates:                                  |                       |              |         |             |
| Moody's Aa Composite<br>(12/31/86)           | 9.00%                 | +            | .02     | — 1.69      |
| 30-Day Visible Supply<br>(\$ Million)        | \$3,233               | — \$         | 503     | +\$2,583    |
| Stocks:                                      |                       |              |         |             |
| Dow-Jones Averages:                          |                       |              |         |             |
| Industrials                                  | 1,900.03              | —            | 26.85   | +350.83     |
| Transportation                               | 805.35                | —            | 15.02   | +102.36     |
| Utilities                                    | 205.67                | —            | 4.31    | + 29.79     |
| 65 Stocks                                    | 737.08                | —            | 12.11   | +120.58     |
| N.Y.S.E. Composite Index                     | 138.65                | —            | 2.35    | + 17.15     |
| N.Y.S.E. Avg. Daily Vol.<br>for Week (000's) | 112,990               | —            | 10,565  | +10,750     |

\*46% Taxable equivalent 12.61%.

† Bond equivalent.

### International Rates

|                                   | Wednesday<br>12/31/86 | Week<br>Ago             |
|-----------------------------------|-----------------------|-------------------------|
| EURODOLLAR<br>DEPOSIT RATES (bid) |                       |                         |
| Overnight                         | 15.00%                | 6.13%                   |
| 1 month                           | 6.56                  | 7.75                    |
| 3 month                           | 6.25                  | 6.50                    |
| 6 month                           | 6.19                  | 6.25                    |
| 1 year                            | 6.19                  | 6.19                    |
| EURODOLLAR BONDS                  |                       |                         |
| Average Yield                     |                       |                         |
| Medium Term (5 to 7 yrs.)         | 7.17%                 | 7.13%                   |
| Long Term (7 to 15 yrs.)          | 7.97                  | 7.93                    |
| FOREIGN EXCHANGE SPOT RATES       |                       |                         |
| New York Opening<br>(12/31/86)    | U.S. \$<br>Equivalent | Currency<br>Per U.S. \$ |
| Canada                            | .7245                 | 1.3803                  |
| France                            | .1556                 | 6.4250                  |
| Germany                           | .5187                 | 1.9280                  |
| Italy                             | .0007440              | 1344.00                 |
| Japan                             | .006306               | 158.57                  |
| Mexico                            | .001083               | 923.00                  |
| Switzerland                       | .6200                 | 1.6130                  |
| U.K.                              | 1.4790                | .6760                   |

| MH TRADE-WEIGHTED DOLLAR* (12/31/86) | Change Since |         |
|--------------------------------------|--------------|---------|
|                                      | Week Ago     | 2/27/85 |
|                                      | —0—          | —7.6%   |

\*Adjusted for inflation

will cause lasting changes to America and its economy. Fewer households will be able to participate in building home equity, and the need for two incomes will become the norm in American households.

Already, the affordability of local housing has created problems in filling certain jobs in tight labor markets. The Long Island Regional Planning Board estimates that at an annual salary of \$34,000, a computer analyst would have to devote 45 percent of his or her salary to make payments on a house in Nassau County; an electronics technician would have to use 77 to 81 percent.

A final, more serious aspect of the growing unaffordability of housing is the consequences of excluding a larger and larger proportion of Americans from homeownership—a rite of financial passage that has been considered a fundamental right in postwar America. With the price of homes skyrocketing at a double-digit annual pace, this disenfranchisement will not only affect poor families, but will increasingly frustrate middle-class Americans who may find themselves with good-paying jobs but without the ability to purchase and own a home.

## Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

|                               | Week Ending<br>12/24/86 | S Chngs Since<br>Week Ago Year Ago        |         |
|-------------------------------|-------------------------|-------------------------------------------|---------|
| Reserve Bank Credit           |                         |                                           |         |
| U.S. Gov'ts and Agencies      |                         |                                           |         |
| Owned Outright & RPs          | 208.704                 | + 2.080                                   | +21.090 |
| Loans to Depository Inst.     | .554                    | - .090                                    | - .394  |
| Float                         | 1.482                   | + .388                                    | + .092  |
| Total Reserve Bank Credit     | 227.146                 | + 2.670                                   | +22.5C5 |
| Treasury Deposits with        |                         |                                           |         |
| Federal Reserve Banks         | 3.391                   | - .133                                    | - .186  |
| Currency in Circulation       | 209.785                 | + 1.416                                   | +13.841 |
| Gov'ts held for Foreign Acct. |                         |                                           |         |
| by F.R. Banks (End-of-Week)   | 163.173                 | - 1.591                                   | - 2.723 |
| Member Bank Reserves:         | 12/17/86                |                                           |         |
| Total Reserves Held           | 55.909                  | + 1.228                                   | + 9.492 |
| Excess (Deficiency)           | .725                    | - .432                                    | - .103  |
| Net Free Reserves             | .521                    | - .394                                    | + .010  |
| Monetary Aggregates †         |                         | % Change Since<br>3 Months' Ago* Year Ago |         |
| M1 (12/15/86)                 | 722.5                   | + 15.7‡                                   | + 15.2‡ |
| M2 (November '86)             | 2,780.6                 | + 8.3                                     | + 9.0   |
| M3 (November '86)             | 3,460.3                 | + 7.0                                     | + 8.8   |
| Domestic Nonfinancial Debt    | 7,181.0                 | + 11.5                                    | + 13.1  |
| (2nd Q'86)                    |                         |                                           |         |

†Seasonally adjusted.

\* Seasonally adjusted annual rate.  
‡ Four-week moving average.

## New York Money Market

| Offering Rates 12/31/86                                  | 3 Months                  | 6 Months        | 1 Year |
|----------------------------------------------------------|---------------------------|-----------------|--------|
| ‡ U.S. Treasury Bills                                    | 5.70%                     | 5.64%           | 5.66%  |
| * Federal Agencies                                       | 6.00                      | 5.95            | 5.85   |
| * Municipal Notes—High Grade<br>(46% Taxable Equivalent) | 7.22                      | 6.76            | 7.41   |
| Negotiable Time CDs                                      |                           |                 |        |
| Manufacturers Hanover                                    | Rates By Arrangement      |                 |        |
| * Secondary Market—Prime                                 | 6.00                      | 6.00            | 6.05   |
| ‡ Finance Company Paper—Prime                            | ‡* Bankers' Acceptances   |                 |        |
| 5- 14 days                                               | 10.00%                    | Jan.            | 7.50%  |
| 15- 29 days                                              | 7.50                      | Feb.            | 6.75   |
| 30- 59 days                                              | 7.00                      | Mar.            | 6.30   |
| 60- 89 days                                              | 6.15                      | Apr.            | 6.25   |
| 90-179 days                                              | 6.10                      | May             | 6.15   |
| 180-239 days                                             | 6.00                      | Jun.            | 6.05   |
| 240-270 days                                             | 6.00                      |                 |        |
| ‡ Industrial Paper—Prime                                 |                           |                 |        |
| 30- 89 days                                              | 7.25%                     | † Federal Funds |        |
| 90-120 days                                              | 6.40                      | Effective Rate  | 20.0%  |
| ‡ Discount basis.                                        | *Subject to availability. |                 |        |
|                                                          | † Estimated.              |                 |        |

## Selected Business Indicators

(All Dollar Figures in Billions)

|                                                 | Latest Period or<br>End of Period |             | Previous<br>Period | Year Ago<br>Period |
|-------------------------------------------------|-----------------------------------|-------------|--------------------|--------------------|
| Gross National Product (Current Dollars)*       | 3rd Q'86                          | \$ 4,241    | \$ 4,176           | \$ 4,031           |
| Gross National Product (1982 Dollars)*          | 3rd Q'86                          | \$ 3,686    | \$ 3,661           | \$ 3,604           |
| Percent Change, Annual Rate                     | 3rd Q'86                          | 2.8         | 0.6                | 4.1                |
| Change in Consumer Prices*                      | Nov '86                           | 0.3%        | 0.2%               | 0.6%               |
| Change in Producer Prices*                      | Nov '86                           | 2.4%        | 3.6%               | 8.4%               |
| Civilian Employment (Thousands of Persons) †    | Nov '86                           | 110,371     | 110,240            | 107,969            |
| Unemployment as % of Civilian Labor Force †     | Nov '86                           | 7.0%        | 7.0%               | 7.0%               |
| Personal Income*                                | Nov '86                           | \$ 3,531    | \$ 3,520           | \$ 3,372           |
| Leading Indicators Composite Index (1967=10C) † | Nov '86n                          | 182.5       | 180.4r             | 171.6              |
| Industrial Production Index (1977=100) †        | Nov '86                           | 125.9       | 125.2              | 124.8              |
| Net Change in Consumer Installment Credit †     | Oct '86                           | \$ 6.78     | \$ 7.72            | \$ 6.56            |
| U.S. Merchandise Trade Balance                  | Nov '86n                          | -\$ 19.22   | -\$ 14.71r         | -\$ 12.78          |
| Plant and Equipment Expenditures*               | 1st Q'87                          | \$386.82(a) | \$394.34(a)        | \$377.94           |
| Private Housing Starts (Thousands of Units)*    | Nov '86                           | 1,598       | 1,628              | 1,654              |
| New Construction Expenditures*                  | Oct '86                           | \$ 386.5    | \$ 380.3           | \$ 374.0           |
| Total Business Inventories †                    | Oct '86                           | \$ 591.3    | \$ 588.1           | \$ 582.0           |
| Total Business Sales †                          | Oct '86                           | \$ 435.3    | \$ 442.2           | \$ 426.1           |

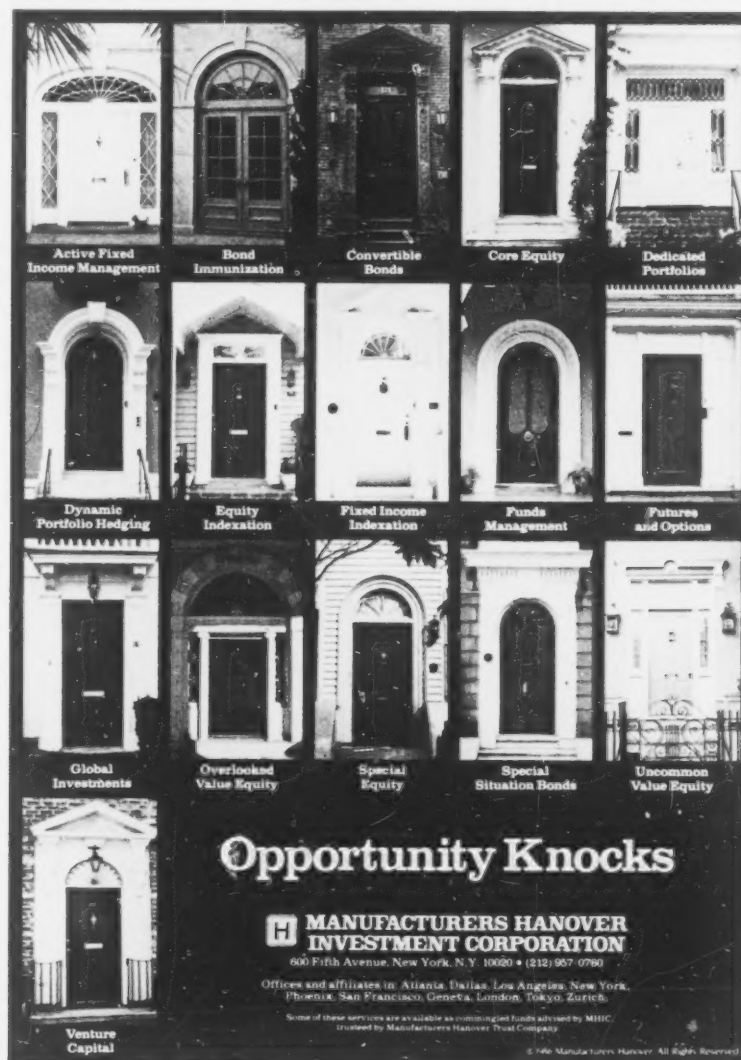
\*Seasonally adjusted annual rate.

†Seasonally adjusted.

n-Newly reported figure.

r-Revised.

a-Anticipated.



|                                   |                            |                            |                            |                          |
|-----------------------------------|----------------------------|----------------------------|----------------------------|--------------------------|
| Active Fixed<br>Income Management | Bond<br>Immunization       | Convertible<br>Bonds       | Core Equity                | Dedicated<br>Portfolios  |
| Dynamic<br>Portfolio Hedging      | Equity<br>Indexation       | Fixed Income<br>Indexation | Funds<br>Management        | Futures<br>and Options   |
| Global<br>Investments             | Overlooked<br>Value Equity | Special<br>Equity          | Special<br>Situation Bonds | Uncommon<br>Value Equity |
| Venture<br>Capital                |                            |                            |                            |                          |

**Opportunity Knocks**

**MANUFACTURERS HANOVER  
INVESTMENT CORPORATION**  
600 Fifth Avenue, New York, N.Y. 10020 • (212) 957-0780

Offices and affiliates in: Atlanta, Dallas, Los Angeles, New York,  
Phoenix, San Francisco, Geneva, London, Tokyo, Zurich.

Some of these services are available as commingled funds advised by MHIC,  
trusted by Manufacturers Hanover Trust Company.

© 1986 Manufacturers Hanover. All Rights Reserved.



Manufacturers Hanover Corporation  
Bank Window, Church St. Station  
New York, N.Y. 10015

First Class Mail  
U.S. Postage  
**PAID**  
New York, N.Y.  
Permit No. 585